

## Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended and P.A. 71 of 1919, as amended.

Local Unit of Government Type <input type="checkbox"/> County <input type="checkbox"/> City <input type="checkbox"/> Twp <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Unit Name No Houghton County Water & Sewage Auth	County Houghton
Fiscal Year End December 31, 2006	Opinion Date June 6, 2007	Date Audit Report Submitted to State June 18, 2007	

We affirm that:

We are certified public accountants licensed to practice in Michigan.

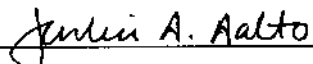
We further affirm the following material, "no" responses have been disclosed in the financial statements, including the notes, or in the Management Letter (report of comments and recommendations).

YES NO Check each applicable box below. (See instructions for further detail.)

1. ☒ ☐ All required component units/funds/agencies of the local unit are included in the financial statements and/or disclosed in the reporting entity notes to the financial statements as necessary.
2. ☒ ☐ There are no accumulated deficits in one or more of this unit's unreserved fund balances/unrestricted net assets (P.A. 275 of 1980) or the local unit has not exceeded its budget for expenditures.
3. ☒ ☐ The local unit is in compliance with the Uniform Chart of Accounts issued by the Department of Treasury.
4. ☒ ☐ The local unit has adopted a budget for all required funds.
5. ☒ ☐ A public hearing on the budget was held in accordance with State statute.
6. ☒ ☐ The local unit has not violated the Municipal Finance Act, an order issued under the Emergency Municipal Loan Act, or other guidance as issued by the Local Audit and Finance Division.
7. ☒ ☐ The local unit has not been delinquent in distributing tax revenues that were collected for another taxing unit.
8. ☒ ☐ The local unit only holds deposits/investments that comply with statutory requirements.
9. ☒ ☐ The local unit has no illegal or unauthorized expenditures that came to our attention as defined in the *Bulletin for Audits of Local Units of Government in Michigan*, as revised (see Appendix H of Bulletin).
10. ☒ ☐ There are no indications of defalcation, fraud or embezzlement, which came to our attention during the course of our audit that have not been previously communicated to the Local Audit and Finance Division (LAFD). If there is such activity that has not been communicated, please submit a separate report under separate cover.
11. ☐ ☒ The local unit is free of repeated comments from previous years.
12. ☒ ☐ The audit opinion is UNQUALIFIED.
13. ☒ ☐ The local unit has complied with GASB 34 or GASB 34 as modified by MCGAA Statement #7 and other generally accepted accounting principles (GAAP).
14. ☒ ☐ The board or council approves all invoices prior to payment as required by charter or statute.
15. ☒ ☐ To our knowledge, bank reconciliations that were reviewed were performed timely.

If a local unit of government (authorities and commissions included) is operating within the boundaries of the audited entity and is not included in this or any other audit report, nor do they obtain a stand-alone audit, please enclose the name(s), address(es), and a description(s) of the authority and/or commission.

I, the undersigned, certify that this statement is complete and accurate in all respects.

We have enclosed the following:		Enclosed	Not Required (enter a brief justification)	
Financial Statements		<input checked="" type="checkbox"/>		
The letter of Comments and Recommendations		<input checked="" type="checkbox"/>		
Other (Describe)		<input type="checkbox"/>		
Certified Public Accountant (Firm Name) Jackie A. Aalto, CPA		Telephone Number (906) 337-2727		
Street Address 200 Fifth Street, Suite 104		City Calumet	State MI	Zip 49913
Authorizing CPA Signature 		Printed Name Jackie A. Aalto		License Number 1101022394

**NORTH HOUGHTON COUNTY WATER  
AND SEWAGE AUTHORITY**

**FINANCIAL REPORT**

Year ended December 31, 2006

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## INDEPENDENT AUDITOR'S REPORT

### Board Members

North Houghton County Water and Sewage Authority  
Calumet, Michigan

I have audited the accompanying basic financial statements of the North Houghton County Water and Sewage Authority as of and for the year ended December 31, 2006 as listed in the table of contents. These financial statements are the responsibility of the Authority's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that I plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. I believe that my audit provides a reasonable basis for my opinion.

In my opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of the North Houghton County Water and Sewage Authority, as of December 31, 2006, and the changes in financial position and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, I have also issued my report dated June 6, 2007 on my consideration of the North Houghton County Water and Sewage Authority's internal control over financial reporting and on my tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of my testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of my audit.

The management's discussion and analysis (identified in the table on contents) is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. I have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, I did not audit the information and express no opinion on it.

My audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the North Houghton County Water and Sewage Authority's basic financial statements. The supplementary information (identified in the table of contents) is presented for purposes of additional analysis and is not a required part of the basic financial statements. The supplementary information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in my opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

A handwritten signature in cursive script that reads "Jackie A. Aalto".

Jackie A. Aalto, CPA

Calumet, Michigan  
June 6, 2007

## **North Houghton County Water and Sewage Authority**

### **Management's Discussion and Analysis Year ended December 31, 2006**

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This section of the annual financial report of the North Houghton County Water and Sewage Authority (the "Authority") presents our discussion and analysis of the entity's financial performance for the year ended December 31, 2006. This discussion should be read in conjunction with the financial statements which follow.

#### **Overview of the Financial Statements**

Management's Discussion and Analysis introduces the Authority's financial statements. The financial statements include all the statements required by the Governmental Accounting Standards Board and the notes to the financial statements. The Authority also includes in this report additional information to supplement the basic financial statements.

#### ***Government-wide Financial Statements***

The Authority's annual reports include two Authority-wide financial statements. These statements provide both long-term and short-term information about the Authority's overall status. Financial reporting at this level uses a perspective similar to that found in the private sector with its basis in full accrual accounting and elimination or reclassification of internal activities.

The first of these statements is the Statement of Net Assets. This is the Authority-wide statement of position presenting information that includes all the Authority's assets and liabilities, with the difference reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Authority as a whole is improving or deteriorating. Evaluation of the overall health of the Authority may extend to various non-financial factors as well.

The second government-wide statement is the Statement of Revenues, Expenses and Changes in Net Assets which reports how the Authority's net assets changed during the current fiscal year. The design of this statement is to show the financial reliance of the Authority's distinct activities or functions on the revenues generated by the Authority.

The Authority's financial reporting includes all the funds of the Authority (primary government) and, additionally, organizations for which the Authority is accountable (component units). Since the Authority's sole purpose is to operate and manage a sewer system, only one fund is maintained. Thus, there are no fund financial statements prepared by the Authority.

#### ***Notes to the financial statements***

The accompanying notes to the financial statements provide information essential to a full understanding of the financial statements.

## ***Other Information***

In addition to the financial statements and accompanying notes, this report also presents certain supplementary information. Other supplementary information includes a budget to actual reconciliation for current year Authority operations.

## ***Financial Overview***

Net capital assets increased \$1,875,508 or 15.00 percent. This net increase was primarily due to capital contributions of the Wolverine/Kearsarge sewer system and land for \$2,066,425 from the Charter Township of Calumet, Michigan and a private land donation of 280 acres in Centennial Heights for \$140,000. The Authority also purchased \$44,495 in capital assets. These increases were offset by \$375,412 in depreciation expense. Total assets increased by \$1,860,300 or 13.66 percent. This increase in total assets is primarily the result of the increase in the aforementioned net capital assets.

Total liabilities increased \$2,462 or less than 1.00 percent. The Authority issued \$131,000 in bonds to pay off the debt on the donated sewer system from the Charter Township of Calumet, Michigan and repaid \$129,000 on outstanding debt. Net assets increased by \$1,857,838 or 35.30 percent.

Operating revenues were \$869,696 an increase of 13.28 percent from 2005. Operating expenses of \$759,781 were up 6.58 percent from 2005 mainly due to an increase in supplies and maintenance. Sewer fees from residential and commercial customers in the Authority's service area comprised most of the revenue collected during the year.

The Authority generates cash from sanitary sewage fees based on water usage and a flat monthly service charge charged to its customers. It uses the cash to pay for current operations and to pay the interest and principal on long-term bonds issued to construct the sanitary sewage system. In 2006, net cash decreased \$23,127 or 4.96 percent.

Sewage rates were increased in the beginning of 2006 and again in 2007 to a level which the Authority believes will be sufficient for the Authority's operations and debt service for the coming year. The Authority believes that it is in substantial compliance with all relevant federal and state requirements for the operation of a sanitary sewage system. A large decrease in water usage would impact the Authority's revenue, which could result in additional rate increases in the future. The Authority is not aware of any circumstances that would cause a significant reduction in water usage. As discussed in Note 7 to the Financial Statements, one customer accounted for 10.63 percent of the Authority's 2006 revenue. Should this one customer significantly lower its water usage, it could have an impact on the financial performance of the Authority and could result in increased rates for the remainder of the customer base. The Authority is not aware of any plans by the customer to significantly alter its water usage at the present time.

## **Financial Analysis of the Authority as a Whole**

The following tables provide a summary of the Authority's financial activities and changes in net assets:

**North Houghton County Water and Sewage Authority**  
**Summary of Net Assets**

	<u>12/31/06</u>	<u>12/31/05</u>
Current and other assets	\$ 302,212	\$ 346,898
Restricted assets	713,951	692,754
Deferred charges	79,514	71,233
Capital assets, net	<u>14,385,909</u>	<u>12,510,401</u>
Total assets	<u>15,481,586</u>	<u>13,621,286</u>
Accounts payable and other current liabilities	181,170	166,708
Revenue bonds payable	<u>8,180,000</u>	<u>8,192,000</u>
Total liabilities	<u>8,361,170</u>	<u>8,358,708</u>
Net assets:		
Invested in capital assets, net of related debt	6,064,909	4,191,401
Restricted for debt service	682,816	661,641
Unrestricted	<u>372,691</u>	<u>409,536</u>
Total net assets	<u>\$ 7,120,416</u>	<u>\$ 5,262,578</u>

**North Houghton County Water and Sewage Authority**  
**Summary of Changes in Net Assets**

	<u>12/31/06</u>	<u>12/31/05</u>
Operating revenues	\$ 869,696	\$ 767,762
Operating expenses	<u>759,781</u>	<u>712,896</u>
Operating income	109,915	54,866
Nonoperating revenues (expenses), net	(349,604)	(300,266)
Capital contributions	<u>2,097,527</u>	<u>                    </u>
Change in net assets	1,857,838	(245,400)
Net Assets - Beginning	<u>5,262,578</u>	<u>5,507,978</u>
Net Assets - Ending	<u>\$ 7,120,416</u>	<u>\$ 5,262,578</u>

**Contacting the Authority's Management**

This financial report is designed to provide taxpayers, creditors, investors and customers with a general overview of the Authority's finances and to demonstrate the Authority's accountability for the revenues it receives. If you have questions concerning this report please contact Mr. Paul Lehto, Chairman, 25880 Red Jacket Road, Calumet, Michigan 49913.



# NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY

## Statement of Net Assets

December 31, 2006

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ASSETS		
CURRENT ASSETS:		
Cash	\$ 20,714	
Investments	1,729	
Accounts receivable, net	244,112	
Interest receivable	2,801	
Inventory	9,346	
Prepays	<u>23,510</u>	\$ 302,212
NONCURRENT ASSETS:		
Restricted Assets:		
Cash	422,443	
Investments	<u>291,508</u>	713,951
Deferred charges		79,514
Capital assets not being depreciated	399,979	
Capital assets being depreciated, net of accumulated depreciation	<u>13,985,930</u>	<u>14,385,909</u>
Total Assets		<u>15,481,586</u>
LIABILITIES		
CURRENT LIABILITIES:		
Accounts payable	6,839	
Accrued expenses	2,196	
Payable from restricted assets:		
Accrued interest	31,135	
Current maturities on revenue bonds	<u>141,000</u>	181,170
NONCURRENT LIABILITIES:		
Revenue bonds payable		<u>8,180,000</u>
Total Liabilities		<u>8,361,170</u>
NET ASSETS		
NET ASSETS:		
Invested in capital assets, net of related debt	6,064,909	
Restricted for debt service	682,816	
Unrestricted	<u>372,691</u>	
Total Net Assets		<u>\$ 7,120,416</u>

The notes to the financial statements are an integral part of this statement.

# **NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY**

## **Statement of Revenues, Expenses and Changes in Net Assets**

**For the year ended December 31, 2006**

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### **OPERATING REVENUES:**

Sewer user fees	\$ 861,810
Other services	3,360
Miscellaneous	<u>4,526</u>

Total Operating Revenues	<u>869,696</u>
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### **OPERATING EXPENSES:**

Salaries, wages & benefits	191,790
Administration	18,116
Supplies & maintenance	113,292
Utilities	31,666
Insurance	29,505
Depreciation	<u>375,412</u>

Total Operating Expenses	<u>759,781</u>
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Operating Income	<u>109,915</u>
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### **NONOPERATING REVENUES (EXPENSES):**

Interest income	35,985
Interest expense	(376,661)
Unrealized loss on investments	(6,506)
Amortization of bond issuance costs	<u>(2,422)</u>

Total Nonoperating Revenues (Expense)	<u>(349,604)</u>
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Income (loss) before contributions	(239,689)
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Capital contributions	<u>2,097,527</u>
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Change in Net Assets	1,857,838
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NET ASSETS – Beginning	<u>5,262,578</u>
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NET ASSETS – Ending	<u>\$ 7,120,416</u>
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The notes to the financial statements are an integral part of this statement.

# NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY

## Statement of Cash Flows

For the year ended December 31, 2006

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### CASH FLOWS FROM OPERATING ACTIVITIES

Receipts from customers	\$ 865,390
Payments to employees	(191,474)
Payments to suppliers	<u>(193,869)</u>

Net cash provided (used) by operating activities	<u>480,047</u>
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### CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES

Proceeds from capital debt	6,875
Capital contributions	15,227
Purchase of capital assets	(55,199)
Principal paid on capital debt	(129,000)
Interest paid on capital debt	<u>(376,639)</u>

Net cash provided (used) by capital and related financing activities	<u>(538,736)</u>
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### CASH FLOWS FROM INVESTING ACTIVITIES

Interest received	<u>35,562</u>
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Net decrease in cash	(23,127)
CASH – Beginning	<u>466,284</u>

CASH – Ending	<u>\$ 443,157</u>
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### RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES

Operating income	\$ 109,915
Adjustments to reconcile operating income to net cash provided (used) by operating activities:	
Depreciation	375,412
Increase in accounts receivable	(4,306)
Increase in inventory	(546)
Increase in prepaids	(868)
Increase in accounts payable	124
Increase in accrued expenses	<u>316</u>

Net cash provided (used) by operating activities	<u>\$ 480,047</u>
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### Noncash investing, capital & financing activities:

Revenue bonds issued to pay off debt on capital contribution	\$ 124,125
Contributions of capital assets	\$ 2,097,527

The notes to the financial statements are an integral part of this statement

# **NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY**

## **Notes to Financial Statements**

**December 31, 2006**

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### **Note 1 – Summary of Significant Accounting Policies**

#### **A. Reporting Entity**

The North Houghton County Water and Sewage Authority was formed in 1983 for the purpose of constructing and making improvements to waste water collection, transmission, and treatment facilities within the service area of the Authority. It operates under a seven member board consisting of two members from the Village of Laurium, one member from Osceola Township, one member from the Village of Calumet and three members from the Charter Township of Calumet. Financial activity of the Authority began during 1986. In 1989, the Authority acquired an existing sewage system from the Village of Laurium. It also purchased sewer lines from a local water company in 1990. The Authority completed sewer system improvement projects in 1993, 1995, 2002 and 2003 with funding provided by various sources. During the current year, the Charter Township of Calumet, Michigan donated the Wolverine/Kearsarge sewer system and land to the Authority.

#### **B. Basis of Presentation**

The Authority records its financial activity under the proprietary fund type, and within the category of an enterprise fund. The Enterprise Fund accounts for operations: (a) that are financed and operated in a manner similar to private business enterprises where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

#### **C. Measurement Focus/Basis of Accounting**

Measurement focus refers to what is being measured; basis of accounting refers to when revenues and expenses are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurement made, regardless of the measurement focus applied. The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting in accordance with generally accepted accounting principles. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of the related cash flows. The Authority applies all GASB pronouncements as well as the FASB pronouncements issued on or before November 30, 1989 unless those pronouncements conflict with or contradict GASB pronouncements.

The statement of activities distinguishes operating revenue and expenses from nonoperating items. Operating revenue and expenses generally result from providing services in

# **NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY**

## **Notes to Financial Statements**

**December 31, 2006**

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connection with the Authority's principal ongoing operations. The Authority's principal operating revenue relates to charges for sewage collection services. Operating expenses include the cost of services, administrative expenses, and depreciation on capital assets. All revenue and expenses not meeting this definition are reported as nonoperating revenue and expenses.

### **D. Cash, Cash Equivalents and Investments**

For purposes of the statement of cash flows, demand deposits and short-term investments with maturities of three months or less when acquired are considered to be cash equivalents. In addition, the statement of cash flows includes both restricted and unrestricted cash and cash equivalents. Investments are reported at fair value, based on quoted market prices and include U.S. Treasury notes, bonds and certificates of deposit with maturities of three months or more. The Authority had no cash equivalents at December 31, 2006.

### **E. Accounts Receivable**

Receivables for sewer fees are shown net of an allowance for uncollectibles, where applicable.

### **F. Inventory and Prepaids**

Inventory is valued at the lower of cost or market, using the first-in/first-out (FIFO) method. Inventory consists of expendable material held for consumption. The cost is recorded as an expense at the time the inventory material is consumed.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaids.

### **G. Restricted Assets – Cash & Investments**

Certain resources set aside for enterprise fund revenue bonds and interest payments and equipment replacement are classified as restricted assets on the statement of net assets because their use is limited by the applicable bond covenant or by capital contributors.

### **H. Capital Assets**

Capital assets are valued at historical cost or estimated historical cost if actual historical cost is not available. Donated capital assets are valued at their estimated fair value on the date donated. Improvements to capital assets that add to the value of the asset or materially extend the asset's life are capitalized at cost. Interest costs incurred during construction of assets are also capitalized.

# **NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY**

## **Notes to Financial Statements**

**December 31, 2006**

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Land with an original cost of \$10,000, and a sewer system, with an original cost net of depreciation of \$455,718, were transferred to the Authority from the Village of Laurium on July 11, 1989 and were capitalized by the Authority at net book value. During 1990, the Authority obtained the sewage lines that lie within the Authority's boundaries at a cost of \$352,501. However, the purchase price did not include the lines within the Villages of Calumet and Laurium since those lines were donated to the Authority. The estimated fair market value of the donated lines has not been determined. Therefore, no related basis has been recorded in the financial records of the Authority.

Capital assets, other than land, are depreciated over the estimated useful life of the asset using the straight-line method. The estimated useful lives over which capital assets are being depreciated are as follows:

Sewer System	50 years
Building & improvements	40 years
Machinery, equipment & furniture	5 to 7 years
Vehicles	5 years

### **I. Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities; disclosure of contingent assets and liabilities at the date of the financial statements; and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

### **Note 2 – Deposits and Investments**

Michigan Compiled Laws Section 129.91, authorizes the Authority to make deposits and invest in accounts of federally insured banks, credit unions, and savings and loan associations that have offices in Michigan. The Authority is allowed to invest in bonds, securities and other direct obligations of the United States or any agency or instrumentality of the United States; United States government or federal agency obligations; repurchase agreements; bankers' acceptance of United States banks; commercial paper rated within the two highest classifications which mature not more than 270 days after the date of purchase; obligations of the State of Michigan or its political subdivisions which are rated as investment grade; and mutual funds composed of investment vehicles which are legal for direct investment by local units of government in Michigan.

Deposits are in one financial institution in the name of the Authority. The investment policy adopted by the Authority is in accordance with statutory authority.

# NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY

## Notes to Financial Statements

**December 31, 2006**

The Governmental Accounting Standards Board (GASB) Statement No. 3, risk disclosures for the cash deposits at year end are as follows:

Cash & Restricted Cash	
Insured (FDIC)	\$ 441,174
Uninsured	<u>                    </u>
 Total Cash & Restricted Cash	 <u>\$ 441,174</u>

At year end, the carrying amount of cash and restricted cash was \$443,157.

The Governmental Accounting Standards Board (GASB) Statement No. 3, risk disclosures for investments at year end are as follows:

Investment Type	(1)	(2)	(3)	Carrying Amount
Risk Categorized				
U.S. Treasury notes & bonds	\$ 233,237	\$		\$ 233,237
Certificates of deposit	<u>60,000</u>	<u>                    </u>	<u>                    </u>	<u>60,000</u>
 Totals	 <u>\$ 293,237</u>	 <u>\$</u>	 <u>\$</u>	 <u>\$ 293,237</u>

### Risk Categories

1. Insured or registered, or securities held by the entity or its agent in the entity's name.
2. Uninsured and unregistered, with the securities held by the counterparty's trust department or agent in the entity's name.
3. Uninsured and unregistered, with the securities held by the counterparty, or by its trust department or agent but not in the entity's name.

### Note 3 – Components of Restricted Assets

Restricted assets (cash and investments) as of December 31, 2006 and 2005 are as follows:

	Bond & Interest Redemption Funds	Bond Reserve Funds	Equipment Replacement Fund	Totals
Restricted assets 12/31/05	\$ 209,141	\$ 354,075	\$ 129,538	\$ 692,754
Additions (withdrawals), net	<u>5,792</u>	<u>40,253</u>	<u>(24,848)</u>	<u>21,197</u>
Restricted assets 12/31/06	<u>\$ 214,933</u>	<u>\$ 394,328</u>	<u>\$ 104,690</u>	<u>\$ 713,951</u>

# NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY

## Notes to Financial Statements

December 31, 2006

The ordinance authorizing the Sewage Disposal System Revenue Bonds requires that the Authority establish Revenue Bond and Interest Redemption Funds and Bond Reserve Funds in amounts not less than the stated annual requirements. At December 31, 2006 the fund balances are sufficient to satisfy the bond ordinance requirements.

### Note 4 – Summary of Capital Assets

A summary of changes in capital assets for the years ended December 31, 2005 and 2006 follows:

	<u>Balance</u> <u>12/31/05</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance</u> <u>12/31/06</u>
Capital assets not being depreciated:				
Land	\$ 242,105	\$ 157,874	\$ _____	\$ 399,979
Capital assets being depreciated:				
Building & improvements	15,103			15,103
Sewer system	15,288,474	2,048,551		17,337,025
Machinery, equipment & furniture	310,474	27,995	(54,299)	284,170
Vehicles	<u>70,251</u>	<u>16,500</u>	<u>(30,210)</u>	<u>56,541</u>
Total capital assets being depreciated	15,684,302	2,093,046	(84,509)	17,692,839
Accumulated depreciation	<u>(3,416,006)</u>	<u>(375,412)</u>	<u>84,509</u>	<u>(3,706,909)</u>
Total capital assets being depreciated, net	<u>12,268,296</u>	<u>1,717,634</u>	<u>_____</u>	<u>13,985,930</u>
Total capital assets, net	<u>\$12,510,401</u>	<u>\$ 1,875,508</u>	<u>\$ _____</u>	<u>\$14,385,909</u>

#### Capital Contributions:

Land with an original cost of \$17,874 and a sewer system, servicing residents in the Wolverine/Kearsarge area, with an original cost net of depreciation of \$2,048,551, were donated to the Authority from the Charter Township of Calumet, Michigan (the "Township") on August 17, 2006. These assets were capitalized by the Authority at net book value, which approximates fair value. The Authority issued bonds to pay off the Township's bonds outstanding on the sewer system of \$124,125 and received the balance in the checking and reserve accounts of \$15,227 from the Township for a net capital contribution of \$1,957,527.

On August 31, 2006, 280 acres of land were donated to the Authority. This donation was recorded at its fair value of \$140,000.



# NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY

## Notes to Financial Statements

**December 31, 2006**

### Note 5 – Long-Term Debt

#### Revenue Bonds

The Authority issues bonds where it pledges income derived from the acquired or constructed assets to pay debt service. Revenue bonds outstanding at year end are as follows:

	Wastewater System Projects							Totals
	5%	4.5%	4.5%	4.5%	3.25%	4.5%	4.1%to5.05%	
Balance 1/1/06	\$2,230,000	\$ 849,000	\$ 112,000	\$3,985,000	\$ 739,000	\$ 404,000	\$	\$8,319,000
Proceeds							131,000	131,000
Principal payments	<u>(45,000)</u>	<u>(15,000)</u>	<u>(2,000)</u>	<u>(49,000)</u>	<u>(11,000)</u>	<u>(5,000)</u>	<u>(2,000)</u>	<u>(129,000)</u>
Balance 12/31/06	<u>\$2,185,000</u>	<u>\$ 834,000</u>	<u>\$ 110,000</u>	<u>\$3,936,000</u>	<u>\$ 728,000</u>	<u>\$ 399,000</u>	<u>\$ 129,000</u>	<u>\$8,321,000</u>

The annual principal payments on the above bonds, payable on June 1 and December 1 of each year, increase incrementally from \$1,000 to \$220,000. Interest is payable on all bond obligations semi-annually on June 1 and December 1.

Revenue bond debt service requirements to maturity are as follows:

<u>Year ending December 31,</u>	<u>Total</u>	<u>Principal</u>	<u>Interest</u>
2007	\$ 516,034	\$ 141,000	\$ 375,034
2008	513,524	145,000	368,524
2009	515,829	154,000	361,829
2010	512,702	158,000	354,702
2011	513,424	166,000	347,424
2012-2016	2,565,802	952,000	1,613,802
2017-2021	2,549,556	1,176,000	1,373,556
2022-2026	2,539,131	1,464,000	1,075,131
2027-2031	2,379,598	1,679,000	700,598
2032-2036	1,565,931	1,201,000	364,931
2037-2041	<u>1,186,829</u>	<u>1,085,000</u>	<u>101,829</u>
	<u>\$15,358,360</u>	<u>\$ 8,321,000</u>	<u>\$7,037,360</u>

Total interest incurred by the Authority was \$376,661 for the year ended December 31, 2006.

# **NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY**

## **Notes to Financial Statements**

**December 31, 2006**

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### **Note 6 – Retirement Plan – Defined Benefit**

#### Description of Plan and Plan Assets

The Authority is in an agent multiple-employer statewide, defined benefit pension plan with the Municipal Employees' Retirement System (MERS), administered by a nine member Retirement Board. MERS was established to provide retirement, survivor and disability benefits. The service requirement is computed using credited service at the time of termination of membership multiplied by the sum of 2.25 percent times the final average compensation (FAC), with a maximum benefit of 80% of FAC. The most recent period for which actuarial data was available was for the fiscal year ended December 31, 2005.

MERS was originally established under Public Act 135 of 1945, and now operates under Public Act 220 of 1996, and the MERS Plan Document, as revised. Pursuant to Act 220, on August 15, 1996, MERS became an independent public non-profit corporation which is an instrumentality of the participating municipalities and courts. Prior to that time MERS was a component unit of the State of Michigan and operated within the Department of Management and Budget. MERS issues a publicly available financial report that includes financial statements and required supplementary information for the system. That report may be obtained by writing to the MERS at 1134 Municipal Way, Lansing, Michigan 48917.

All permanent employees of the Authority are eligible to participate in the plan upon working at least 10 full work days in a given month. As of December 31, 2005, the most recent report available, the Authority had 4 active covered employees, 0 inactive vested members and 0 retirees and beneficiaries. The annual covered payroll at that date totaled \$100,589 and the Authority's total payroll for all employees was \$126,523.

Under the provisions of the plan, pension benefits vest after 10 years of credited service. Participants may elect normal retirement at age 60 with 10 or more years of credited service or early retirement at age 55 with 15 or more years of service, and at age 50 with 25 or more years of service.

#### Funding Policy

The obligation to contribute to and maintain the system for these employees was established by the Authority's board and does not require employees to contribute to the plan. The Authority is required to contribute at an actuarially determined rate; the rate for 2006 was 11.60%.

#### Annual Pension Cost

During the fiscal year ended December 31, 2006, the Authority's contributions totaling \$12,518 were made in accordance with contribution requirements determined by an actuarial valuation of the plan as of December 31, 2005. The employer contribution rate has been determined based on

# NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY

## Notes to Financial Statements

December 31, 2006

the entry age normal actuarial cost method and are based upon the benefit plan(s) adopted by the Authority. Under the entry age normal cost method, the total actuarially-determined contribution requirement is the sum of the normal cost and the payment required to amortize the unfunded accrued liability over the amortization period of 30 years, less the accelerated funding credit, if available. The employer normal cost is, for each employee, the level percentage-of-salary contribution (from entry age to retirement) required each year to accumulate sufficient assets at the member's retirement to pay for his projected benefit. Significant actuarial assumptions used include a long-term investment yield rate of 8% and annual salary increases of 4.5%, plus a percentage based on age-related scale to reflect merit, longevity and promotional salary increases.

The following information has been prepared to provide the information necessary to comply with GASB Statement Numbers 25 and 27. All entries are based on the actuarial methods and assumptions that were used in the December 31, 2005 actuarial valuation to determine the annual employer contribution amounts. The entry age normal actuarial method was used to determine the entries at disclosure.

### GASB 25 INFORMATION (as of 12/31/05)

Actuarial Accrued Liability	
Retirees and beneficiaries current receiving benefits	\$ 0
Terminated employees not yet receiving benefits	0
Current employees –	
Accumulated employee contributions including allocated investment income	0
Employer financed	<u>176,025</u>
Total Actuarial Accrued Liability	176,025
Net Assets Available for Benefits at Actuarial Value (Market value is \$145,377)	<u>149,311</u>
Unfunded (Overfunded) Actuarial Accrued Liability	26,714

### GASB 27 INFORMATION (as of 12/31/05)

Fiscal year beginning	January 1, 2007
Annual Required Contribution (ARC)	9,276
Amortization Factor Used – Underfunded Liabilities (30 years)	0.053632

### Note 7 – Economic Dependency – Major Customer

The Authority had one customer in 2006 who accounted for more than 10% of total revenue. The following is information regarding this customer for the year ended December 31, 2006.

# **NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY**

## **Notes to Financial Statements**

**December 31, 2006**

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	<u>Amount</u>	<u>% of Total</u>
Annual revenue	\$ 869,696	10.63%

### **Note 8 – Commitments and Contingencies**

The Authority receives Federal and State Grants for specific purposes that are subject to review and audit by Federal and State agencies. Such audits could result in a request for reimbursement by the Federal and State agencies for expenditures disallowed under the terms and conditions of the appropriate agency. In the opinion of the Authority's management, such disallowances, if any, will not be significant to the Authority's financial statements.

### **Note 9 – Risk Management**

The Authority is exposed to various risks of loss related to property loss, torts, errors and omissions, employee injuries, as well as medical benefits provided to employees. All risk of loss is covered by commercial insurance. Settled claims for the commercial insurance have not exceeded the amount of insurance coverage in any of the past 3 years.

## **SUPPLEMENTARY INFORMATION**

**NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY**

**Schedule of Revenues and Expenses – Budget to Actual  
Operations Only**

**For the year ended December 31, 2006**

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	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>
OPERATING REVENUES:			
Sewer user fees	\$ 832,000	\$ 855,000	\$ 861,810
Other	<u>12,200</u>	<u>12,200</u>	<u>7,886</u>
Total Operating Revenues	<u>844,200</u>	<u>867,200</u>	<u>869,696</u>
OPERATING EXPENSES:			
Salaries, wages & benefits	180,000	189,000	191,790
Administration	19,900	17,900	18,116
Supplies & maintenance	85,500	119,200	113,292
Utilities	36,000	33,300	31,666
Insurance	36,000	30,000	29,505
Depreciation	<u>360,000</u>	<u>360,000</u>	<u>375,412</u>
Total Operating Expenses	<u>717,400</u>	<u>749,400</u>	<u>759,781</u>
Operating Income	<u>\$ 126,800</u>	<u>\$ 117,800</u>	<u>\$ 109,915</u>

This schedule is for supplemental information. It is prepared to present revenues and expenses related to current operations only and as such does not present the results of operations on the basis of generally accepted accounting principles.

## **FEDERAL PROGRAMS**

**NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY**  
**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND**  
**ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF**  
**FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH**  
***GOVERNMENT AUDITING STANDARDS***

Board Members  
North Houghton County Water and Sewage Authority  
Calumet, Michigan

I have audited the accompanying basic financial statements of the North Houghton County Water and Sewage Authority, as of and for the year ended December 31, 2006, and have issued my report thereon dated June 6, 2007. I conducted my audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In planning and performing my audit, I considered the North Houghton County Water and Sewage Authority's internal control over financial reporting in order to determine my auditing procedures for the purpose of expressing my opinion on the financial statements but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, I do not express an opinion on the effectiveness of the North Houghton County Water and Sewage Authority's internal control over financial reporting.

My consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, I identified certain deficiencies in internal control over financial reporting that I consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the North Houghton County Water and Sewage Authority's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the North Houghton County Water and Sewage Authority's financial statements that is more than inconsequential will not be prevented or detected by the North Houghton County Water and Sewage Authority's internal control. I consider the deficiencies described in the accompanying schedule of findings and responses as items 2006-01 and 2006-02 to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements



will not be prevented or detected by the North Houghton County Water and Sewage Authority's internal control.

My consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, I believe that the significant deficiencies described above are not material weaknesses.

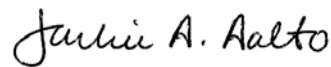
#### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the North Houghton County Water and Sewage Authority's financial statements are free of material misstatement, I performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of my audit, and accordingly, I do not express such an opinion. The results of my tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

I noted certain matters that I reported to management of the North Houghton County Water and Sewage Authority in a separate letter dated June 6, 2007.

North Houghton County Water and Sewage Authority's response to the findings identified in my audit is described in the accompanying schedule of findings and responses. I did not audit the North Houghton County Water and Sewage Authority's response and, accordingly, I express no opinion on it.

This report is intended solely for the information and use of the board membership, management, federal and state awarding agencies, and, if applicable, pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.



Jackie A. Aalto, CPA

Calumet, Michigan  
June 6, 2007

# **NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY**

## **Schedule of Findings and Responses**

**Year ended December 31, 2006**

### **FINDINGS – FINANCIAL STATEMENT AUDIT**

#### **SIGNIFICANT DEFICIENCIES**

##### **2006-01 Internal Control Design**

*Criteria:* The segregation of incompatible financial duties is important to adequately protect the Authority's assets and ensure accurate financial reporting.

*Condition:* Presently there is not an adequate number of personnel available to properly segregate duties to provide reasonable assurance that no one employee would have access to both physical assets and related accounting records, or to all phases of a transaction.

*Effect:* Without proper segregation of duties, the risk increases that errors and fraud could occur and not be detected within a timely basis.

*Cause:* The Authority's limited population and resources result in the inability to provide sufficient staffing to fully segregate incompatible duties.

*Recommendation:* Efficient segregation of duties in a small environment is often difficult; however, I feel that the Authority's board should be aware of the risk associated with this lack of duty segregation and attempt to exercise as much oversight control in these areas as possible and feasible.

*Response:* We concur with the recommendation.

##### **2006-02 Operation of Internal Control**

*Criteria:* The reconciliation of the accounts receivable records of the Authority's outside billing agents to the Authority's records is important to ensure that the Authority's assets and revenues are properly recorded in the financial statements and to ensure that all amounts collected by third parties is remitted to the Authority.

*Condition:* Presently the Authority uses outside parties to bill and collect sewer revenues. The Authority does not reconcile the revenues to amounts remitted to the Authority until the year end audit is performed.

*Effect:* Without reconciling the revenues/billings to the Authority's records on a regular basis there is a risk that monies collected and owed to the Authority are not being remitted to the Authority and that assets and revenues are not being properly recorded in the financial statements.

# **NORTH HOUGHTON COUNTY WATER AND SEWAGE AUTHORITY**

## **Schedule of Findings and Responses**

**Year ended December 31, 2006**

*Cause:* The Authority's limited personnel and resources result in the inability to provide sufficient staffing to reconcile the revenues to the amounts remitted and accounts receivable balances reported to the Authority.

*Recommendation:* The Authority should reconcile the billings, collections and receivables on the bimonthly billing cycles to ensure that all monies collected are remitted to the Authority and that the accounts receivable balance and revenues are properly reported.

*Response:* We concur with the recommendation.

**Board Members**

North Houghton County Water & Sewage Authority  
Calumet, Michigan

In planning and performing my audit of the basic financial statements of the North Houghton County Water and Sewage Authority (the “Authority”) as of and for the year ended December 31, 2006, in accordance with auditing standards generally accepted in the United States of America, I considered the Authority’s internal control over financial reporting (internal control) as a basis for designing my auditing procedures for the purpose of expressing my opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority’s internal control. Accordingly, I do not express an opinion on the effectiveness of the Authority’s internal control.

My consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, I identified certain deficiencies in internal control that I consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects the entity’s ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity’s financial statements that is more than inconsequential will not be prevented or detected by the entity’s internal control. I consider the following deficiencies to be significant deficiencies in internal control.

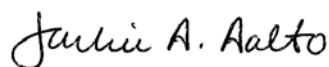
- 1) The segregation of incompatible financial duties is important to adequately protect the Authority’s assets and ensure accurate financial reporting. Presently there is not an adequate number of personnel available to properly segregate duties to provide reasonable assurance that no one employee would have access to both physical assets and related accounting records, or to all phases of a transaction. I feel that the Authority’s board should be aware of the risk associated with this lack of duty segregation and attempt to exercise as much oversight control in these areas as possible and feasible.
- 2) The reconciliation of the accounts receivable records of the Authority’s outside billing agents to the Authority’s records is important to ensure that the Authority’s assets and revenues are properly recorded in the financial statements and to ensure that all amounts collected by third parties is remitted to the Authority. The Authority should reconcile the billings, collections and receivables on the bimonthly billing cycles to ensure that all monies collected is remitted to the Authority and that the accounts receivable balance and revenues are properly reported.

In addition, I noted the following other matters which are not deemed to be internal control deficiencies:

- The Authority should have formal written contracts between itself and its outside billing agents.
- The Authority should review insurance policies to ensure that the coverage provided is adequate for the size of the Authority's operations.
- During 2006, the federal courts deemed the federal excise tax on phone bills to be unconstitutional. They passed a ruling that all entities that paid the excise tax would be eligible for a refund of taxes paid between 2003 and 2006. Management should assess the amounts of tax paid to determine if filing for a refund is warranted.
- Adopt a written conflict of interest policy.
- Adopt a written capitalization policy.
- Ensure that deeds are properly recorded on all property transferred and owned by the Authority.

This communication is intended solely for the information and use of the board membership, management, federal and state awarding agencies, and if applicable, pass-through entities, and others within the organization, and is not intended to be and should not be used by anyone other than these specified parties.

I would like to thank the Authority personnel for their courtesy and assistance during the audit. I appreciate the opportunity to serve as your auditor. If there are any questions about your financial report or the above comments and recommendations, I would be happy to discuss them at your convenience.



Jackie A. Aalto, CPA

Calumet, Michigan  
June 6, 2007